IN THE

Supreme Court of the United States

October Term, 1937.

No. [redacted] 11

Guy T. Helvering, Commissioner of Internal Revenue,
Petitioner,

v.

Robert C. Winmill, *Respondent*.

On Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

BRIEF OF RESPONDENT IN OPPOSITION.

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Opinions Below.

The opinion of the Board of Tax Appeals (R. 17-32) is reported in 35 B. T. A. 804. The opinion of the United States Circuit Court for the Second Circuit is reported in 93 Fed. (2nd) 494.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered December 13, 1937. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

Question Presented.

Whether a taxpayer who is engaged in the business of buying and selling securities for his own account may deduct buying commissions paid to brokers in the purchase of securities both bought and sold during the taxable year.

Statute and Regulation Involved.

Revenue Act of 1932, c. 209, 47 Stat. 169:

> Sec. 23. DEDUCTIONS FROM GROSS INCOME. In computing net income there shall be allowed as deductions:
>
> (a) *Expenses.*—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; * * *

Treasury Regulations 77, promulgated under the Revenue Act of 1932:

> Art. 121. *Business expenses.*—Business expenses deductible from gross income include the ordinary and necessary expenditures directly connected with or pertaining to the taxpxayer's trade or business, except the classes of items which are deductible under the provisions of articles 141-272. The cost of goods purchased for resale, with proper adjustment for opening and closing inventories, is deducted from gross sales in computing gross income. (See article 55.) Among the items included in business expenses are management expenses, commissions, * * *. etc.

Statement.

During the year 1932, the respondent operated three separate securities trading accounts (R. 19). During that year he paid, as brokerage commissions in the purchase of securi-

ties, which he sold during the year 1932, the sum of $7,493.50 (R. 19-20). He also operated jointly with other persons four securities trading accounts. His share of the buying commissions paid by these joint ventures in 1932 was $270. The securities on which these buying commissions were paid were sold during the year 1932 (R. 20). He contends that these amounts are deductible as an ordinary and necessary business expense. The Commissioner of Internal Revenue determined that such commissions represented a part of the cost of the securities, and his action was affirmed by the Board of Tax Appeals (R. 29). Upon appeal, the Circuit Court of Appeals reversed and remanded the cause with instructions to "make a finding as to whether or not the petitioner, in 1932, was a trader in the business of buying and selling securities. If so the commissions for purchases and sales are deductible." (R. 74)

Reasons for Denying the Writ.

The writ should be denied because there is no conflict between the decision of the court below under the 1932 Revenue Act and the decision of the Circuit Court of Appeals for the Fifth Circuit under the 1921 Revenue Act (42 Stat. 237) in *Hutton* v. *Commissioner*, 39 Fed. (2nd) 459. The commissions, as to which the petition for certiorari is directed, would be allowable clearly under the *Hutton* decision. Nor is there a conflict between the decision of the court below and any of the other decisions cited in the petition for certiorari. The decision is correct.

ARGUMENT.

I.

Under the *Hutton* decision the buying commissions in the amounts of $7,493.50 and $270 (as to which the petition for certiorari is directed) clearly would be allowable deductions because the securities on which these commissions were paid were sold during 1932. The court in the *Hutton* case spe-

cifically stated (p. 460) that the commissions paid in purchasing the securities may be deducted when the securities are eventually sold. Certainly certiorari on the ground of conflict with the *Hutton* case cannot be granted to review the deductibility of these commissions.

There is no conflict with *Bonwit Teller & Co.* v. *Commissioner,* 53 Fed. (2nd) 381, certiorari denied, 284 U. S. 690, *Meyran* v. *Commissioner,* 63 Fed. (2nd) 986 (C. C. A. 3rd) or *Commissioner* v. *Chicago Dock & Canal Co.,* 84 Fed. (2nd) 288 (C. C. A. 7th), because the property in each of those cases was a lease, the terms of which, in each case, ran for scores of years and it was anticipated that the benefits of the expenditures of the commissions would extend for many years after the taxable year. These expenditures were clearly in the nature of the capital expenditures intended to be provided for in Article 282 of Regulations 77 and are to be distinguished from the commissions specifically mentioned in Article 121 of Regulations 77, which are "ordinary and necessary expenditures directly connected with or pertaining to the taxpayer's trade or business."

As correctly stated by the court below: "The questions presented in *Helvering* v. *Union Pacific Ry. Co.* (293 U. S. 282) dealt with deductions of commissions on bonds issued by the taxpayer itself. The court there approved the regulations providing for the capitalization of the commissions involved." (R. 74) Clearly therefore there is no conflict with that decision of this court. The commissioner's own regulations recognize that commissions are to be capitalized or expensed according to the purpose for which the property (on which the commission is paid) is acquired. If the property is being bought and sold in carrying on a trade or business, the commission is an expense. I. T. 2305, C. B. V-2, 108, The Highlands Trust, No. 1546, 32 B. T. A. 760. See also *Alexander Sprunt & Sons,* 64 Fed. (2nd) 424; *Kornhauser* v. *United States,* 276 U. S. 145, *Whitman* v. *Commissioner,* 16 B. T. A. 197, affd. 49 Fed. (2nd) 1087. If the property is being bought as a capital investment or to be

used over the years to produce income from such use, the commission is a capital expenditure and the authorities relied upon by the petitioner apply. No set rule can be prescribed based upon the *kind of property* on which the commission is paid. The circumstances and the purpose of acquisition in relation to its use must govern.

II.

While buying commissions on securities *not sold* during the taxable year would be deductible following the broad language of the opinion of the court below, under the 1932 Revenue Act, the disallowance under the 1921 Revenue Act, of such commissions, following the *Hutton* decision, does not constitute a conflict even in a general sense (as distinguished from a specific sense when applied to the particular commissions as to which the petition is addressed.)

Section 214 (a) of the Revenue Act of 1921 is in substance identical with Section 23 (a) of the Revenue Act of 1932 and contains the identical language quoted from the latter statute on page 2 hereof allowing "compensation for personal services" to be deducted. However, the court in the *Hutton* case ignored the plain language of the statute and disallowed the commissions of the taxpayer there, who was "engaged in the business of buying, holding and selling realties, securities, etc."

The reasons relied upon by the court in the *Hutton* case for ignoring the plain language of the act and for affirming what it considered to be the applicable rule of the Treasury Department (under which buying commissions were added to the cost of securities regardless of whether or not the commissions constituted business expenses) were: that the court had been referred to no decision contrary to the rule of the Department (as the court construed it) and that the rule was "fair and reasonable" because the taxpayer "suffers no hardship" by it, as the commissions paid in purchasing the securities may be deducted when the securi-

ties are eventually sold. But these reasons are wholly inapplicable in the instant case. Unless the commissions are deductible as expenses there is a *certainty* of hardship suffered here and not a mere "hazard" as suggested on page 7 of the petition. The court below pointed out that the commissions in issue were paid on shares sold at a loss (R. 71) and said (R. 74):

> The taxpayer suffered no hardship by such a rule as was pointed out in Hutton v. Commr., 39 Fed. 2, 459 (C. C. A. 5), since under the Revenue Acts then in force the commissions would be reflected against income when the securities were eventually sold. But under the 1932 Revenue Act, due to section 23 (r), the commissions paid would not be reflected against gross income unless the sale of the securities resulted in a profit.

Because of these fundamental differences between the 1921 and the 1932 Revenue Acts there is no conflict between the *Hutton* case and the decision of the court below in this case.

This fundamental difference between the Revenue Act of 1932 and the prior revenue acts is caused by Section 23 (r) of the Revenue Act of 1932, which was first introduced in the latter Act. In view of this difference, the Revenue Acts of 1918, 1921, 1924, 1926, 1928 and 1932 cannot be regarded as having given legislative approval to the former regulations as applied to the 1932 Revenue Act, because that Act is so fundamentally different from the earlier acts in the matter of treating deductions for securities losses. It made little or no difference under the earlier acts whether commissions were capitalized or expensed, because they would reduce income in either event. But under the 1932 Act, unless the securities are sold at a profit the commissions can never be deducted if they are not expensed. The rule of legislative approval of department regulations therefore, has no application in the instant case. The wording of the rule as stated in *Brewster* v. *Gage*, 280 U. S. 327,

337, relied upon by the petitioner, demonstrates its own inapplicability. The rule as stated there is:

> The *substantial re-enactment* in later acts of the provision theretofore construed by the Department is persuasive evidence of legislative approval of the regulation. (Emphasis ours)

The rule as stated in *United States* v. *Dakota-Montana Oil Co.*, 288 U. S. 459, 466, and relied upon by the petitioner, also illustrates the point that a "material change" in a subsequent statute destroys, as to that Act, the application of regulations theretofore deemed to have legislative approval. The rule as stated there is:

> The administrative construction must be deemed to have received legislative approval by the re-enactment of the statutory provision, *without material change.* (Emphasis ours)

Conclusion.

The decision of the Circuit Court of Appeals is correct. There is no conflict of authorities and the decision below is fully supported by the facts and by the law. The petition for certiorari should therefore be denied.

Respectfully submitted,

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March 31, 1938.